

Audit Methodologies and/or Other Computational Issues

C. O'Donoghue
Admin. Law Judge

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1. The Department's *prima facie* case, inclusive of all jurisdictional elements, was established by the admission into evidence of the Corrections of Returns, showing a total liability due and owing in the amount of \$51,861.00 for the period from November 1, 1986 until December 31, 1992. Dept. Grp. Ex. No. 1. The correction of returns was incorrect as originally submitted by the auditor, but was corrected by Ms. Stout in Springfield. Tr. pp. 56, 58.

2. There are two separate assessments, one for the delinquencies and one for the deficiencies. A 30% fraud penalty is assessed against the deficiencies and a 30% penalty is assessed against the delinquencies. Both assessments cover the same audit period. Dept. Grp. Ex. No. 1.

3. Taxpayer was the subject of investigation in 1991 by the Department's Special Agent Sam Rossi. Tr. pp. 62, 63. In 1992, Mr. PRESIDENT, the taxpayer's president and stockholder, was convicted of causing a fraudulent transaction reporting return to be filed. Dept. Grp. Ex. No. 2; Tr. p. 16. He was placed on probation for 13 months and paid restitution of \$7800.00. Tr. p. 112. The auditor gave the taxpayer credit for this restitution. Taxpayer Ex. No. 1.

4. Mr. Thompson, the Department auditor, reviewed all transaction reporting returns (ST-556s) filed by the taxpayer for the entire audit period and the available deal jackets which contained documentation for the automobile sales. Tr. pp. 20, 32, 33. Some files contained bills of sale that stated a particular sales price, while the corresponding ST-556 return stated a lower sales price. At times, two bills of sale were found for the same transaction with the ST-556 reflecting the lower sales price. Tr. p. 23.

5. Taxpayer did not record wholesale sales in the police book, a ledger which should contain all transactions. These wholesale sales were also not given a stock number. Tr. p. 75.

6. The auditor scheduled the bank deposits yearly and compared them to the filed ST-556 amounts. The liability was established by taxing the difference found between the bank deposits and the filed ST-556 amounts. Tr. p. 38.

7. Where documentation for the wholesale sale was provided, proper credit was given to the taxpayer, (Tr. p. 39; Taxpayer Ex. No. 1), otherwise the transaction was assumed to be a retail sale. Tr. p. 38. The auditor gave credit for wholesale sales amounting to \$35,890.00 for a two and a half month period in 1992. Tr. p. 43; Taxpayer Ex. No. 1. He did not use that two and a half month period as a sample to develop a resale percentage and apply it to the prior 78 months to determine wholesale sales. The auditor did not use sampling techniques because he was doing a detailed audit. Tr. p. 44.

8. PRESIDENT lowered the sales price on the ST-556. Tr. p. 115. In effect, he was only paying sales tax on the down payment. Tr. p. 115.

9. The deal jacket for a sale to XXXXX on 9/25/89 contained two bills of sale for stock No. 1500 dated 9/25/89. Each reflects a different cash price. Dept. Ex. No. 5; Tr. No. 2. pp. 61, 62. The cash price on one bill of sale is \$1200, the cash price on the second bill of sale states \$100. The ST-556 that was in this file indicates a sales price of \$100.00. Dept. Ex. No. 5; Tr. p. 63.

Conclusions of Law:

The Retailers' Occupation Tax Act, 35 ILCS 120/1 et seq. (hereinafter "ROTA") provides, in pertinent part, that:

It shall be presumed that all sales of tangible personal property are subject to tax under this Act until the contrary is established, and the burden of proving that a transaction is not taxable hereunder shall be upon the person who would be required to remit the tax to the Department if such transaction is taxable.

35 ILCS 120/7.

The auditor had requested all of taxpayer's documentation to substantiate wholesale sales. Tr. p. 43. This documentation and the books and records of

the taxpayer proved inadequate for the verification of wholesale sales made during the audit period. The auditor, therefore, used certain assumptions to determine the tax liability for the years in question. He examined the taxpayer's bank statements to determine total deposits for each year and compared these figures with those reported on filed ST-556 returns. Large differences were uncovered.

Taxpayer contends that the auditor incorrectly determined the taxpayer's liability. Taxpayer's CPA, ACCOUNTANT, accounted for all the cars by stock number during the audit period, then traced the stock number to the sales journal, and to any available ST-556 returns. Taxpayer's accountant, prepared his workpapers based upon the assumption that if a ST-556 was not prepared by the taxpayer the sale must have been at wholesale since filing a ST-556 is required for the purchaser to receive a title and license. This analysis fails to consider that the statute clearly demands that the taxpayer prove sales are nontaxable. This burden is not too large since it is the taxpayer who has the books and records available, not the Department. Careful and complete bookkeeping is all that is required to avoid taxation on truly nontaxable sales. It is illogical to assume that a transaction must have been nontaxable because the taxpayer does not have the required documentation. Taxpayer's analysis is based upon this faulty assumption and therefore his determination of the tax liability must necessarily be disregarded.

Taxpayer claims he was not aware of the necessity of entering wholesale sales into the police book. Further, he testified he did not know he should have even filed ST-556 returns for wholesale sales. I find this testimony implausible. The taxpayer, as a licensed dealer with over forty years of experience, surely was aware that all purchases and sales should have been entered into the police book in accordance with 625 ILCS 5/5401.2. Such a practice might have afforded the auditor some record of wholesale sales.

Moreover, Section 130.540 of the Department's regulations clearly provides that "... with respect to motor vehicles ..., every retailer selling this kind of tangible personal property in Illinois shall file, with the Department, upon a form prescribed and supplied by the Department, a separate return for each such item of tangible personal property which the retailer sells." The return itself contains a section entitled "Complete for Non-taxable Sales" and asks for the purchaser's Illinois Dealer License No. Thus, taxpayer's obligations in this matter were clear.

In addition, the testimony of taxpayer's witnesses, two area auto dealers, regarding PRESIDENT's wholesaling of cars is not persuasive. Their testimony did not address PRESIDENT's failure to provide the Department with documentation of alleged wholesale transactions and thus was not determinative of the issues in the present matter.

Pursuant to Illinois statute and case law, the Correction of Returns is *prima facie* correct and constitutes *prima facie* evidence of the correctness of tax due as shown therein. 35 ILCS 120/4; A.R. Barnes and Co. v. Department of Revenue, 173 Ill. App. 3d 826 (1st Dist. 1988). In order to overcome the presumption of validity attached to the Department's corrected returns the taxpayer "must produce competent evidence, identified with their books and records showing that the Department's returns are incorrect." Copilevitz v. Department of Revenue, 41 Ill. 2d 154 (1968); Masini v. Department of Revenue, 60 Ill. App. 3d 11 (1st. Dist. 1978). Oral testimony, standing alone, is not sufficient to overcome the *prima facie* correctness of the Department's determinations. A.R. Barnes, supra.

The record does not reflect sufficient documentary evidence identified with taxpayer's books and records to overcome the Department's *prima facie* case. Thus, the Department's determinations must stand.

Taxpayer contends that the auditor incorrectly assessed a fraud penalty and thus seeks abatement. PRESIDENT's claim that he was unaware of the requirement

to include the total sales price on the ST-556 and accordingly pay tax on this entire amount lacks credibility. Looking at the tax return, one can see that it clearly indicates on Line 1 "Total Price, including Accessories, Federal Tax and Freight". This instruction appears clear and unambiguous especially in light of PRESIDENT's forty years experience in the automobile industry.

In Vitale v. Illinois Department of Revenue, 118 Ill. App. 3d 210 (3rd Dist. 1983), the appellate court affirmed a fraud penalty based on underreported sales. In Vitale, the court found circumstantial evidence sufficient to show intent where the taxpayer's bank deposits exceeded his gross receipts by \$25,000 a year and the plaintiff had failed to maintain business records or to explain his underpayment of taxes. *Id.* at 213.

In the case at hand, a fraud penalty was also assessed based on underreported receipts. The auditor indicated on his audit report that credit was given for resales where documentation was provided by the taxpayer. Even giving such credit, the auditor's schedules reflect that over the course of the audit period taxpayer had underreported sales of over \$500,000. These underreported sales covered the entire audit period, a period of approximately six years. The amount of underreported receipts, the fact that they extend over a lengthy period of time and the lack of sufficient documentation reflects an inference of intent and fraud, not mere mistake. Testimony was also given that during review of the deal jackets it was often discovered that the same transaction had two bills of sale, each with a different sales price. The lower sales price was then reflected on the filed ST-556. Such conduct seems to indicate that taxpayer knew his filing method was wrong and took actions to avoid detection. Further, PRESIDENT's conviction of causing a fraudulent transaction reporting return to be filed is clear evidence that PRESIDENT's actions went beyond mere mistake and thus, I find that the fraud penalty was properly assessed.

WHEREFORE, for the reasons set forth above, it is my recommendation that NTL Nos. XXXXX and XXXXX be finalized as issued.

Christine O'Donoghue
Administrative Law Judge